



Commissioner of Domestic Taxes v H. P. Gauff Ingenieure GMBH Company Limited (Tax Appeal E057 of 2020) [2021] KEHC 206 (KLR) (Commercial and Tax) (3 November 2021) (Judgment)

Neutral citation: [2021] KEHC 206 (KLR)

**REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
TAX APPEAL E057 OF 2020
DAS MAJANJA, J
NOVEMBER 3, 2021**

BETWEEN

COMMISSIONER OF DOMESTIC TAXES APPELLANT

AND

H. P. GAUFF INGENIEURE GMBH COMPANY LIMITED RESPONDENT

(Being an appeal against the judgment of the Tax Appeals Tribunal at Nairobi dated 30th March 2021 in Tax Appeal No. 165 of 2017)

JUDGMENT

Introduction and Background

1. The Appellant (“the Commissioner”) appeals against the judgment of the Tax Appeals Tribunal (“the Tribunal”) dated 30th March 2020. The Respondent, is the Kenyan branch of a German multi-sectoral firm of engineering consultants that delivers solutions in a wide range of professional disciplines.
2. The facts giving rise to this appeal can be traced back to a verification exercise conducted by the Commissioner on the Respondent’s tax affairs and compliance status for the period from January 2014 to December 2016. The Commissioner communicated its findings to the Respondent in a letter dated 19th June 2017 where it issued additional tax assessments of KES 42,813,069.00 and KES 12,825,707.00 under the tax heads of Value Added Tax (“VAT”) and Pay As You Earn (“PAYE”) respectively inclusive of penalties and interest. In its response to the findings, the Respondent, in a letter dated 18th July 2017 conceded to the principal tax assessments of KES 8,929,667.00 and KES 167,695.00 in respect of its PAYE and VAT obligations respectively but formally objected to the VAT assessment of KES 42,645,374.00 through its letter 28th August 2017.



3. The Commissioner, through its letter dated 4th October 2017 dismissed the Respondent's objection and affirmed its earlier assessment on VAT ("the Objection Decision"). Aggrieved by the Objection Decision, the Respondent filed an appeal at the Tribunal, which after hearing the parties' arguments issued interim orders staying the tax demanded by the Commissioner and directing the Respondent to seek the completion of obtaining an exemption certificate within 120 days of the Tribunal's judgment.
4. The Commissioner appeals against this decision and has filed written submissions in support thereof in addition to its Memorandum of Appeal. The Respondent opposes the appeal through its Statement of Facts dated 2nd March 2021 and written submissions.

The Commissioner's Submissions

5. Before the Tribunal, the Commissioner submitted that it made the decision to charge VAT on the projects being undertaken by the Respondent to the Kenya National Highways Authority ("KenHA") and the Ministry of Roads as it did not have exemption certificates. The Commissioner adds that the Respondent dealt with both exempt and taxable supplies and that the inputs directly relating to the exempt supplies were disallowed and the common inputs apportioned accordingly, which gave rise to the adjustment and assessment of KES 42,813,069.00.
6. The Commissioner contended that the Respondent did not have a remission certificate to provide the services free of VAT and that it only provided proforma invoices for the purpose of processing VAT exemption certificates. The Commissioner reiterated that the supplies to KenHA and the Ministry of Roads were treated as taxable and VAT charged and that it did not add additional amounts assessed in the Objection Decision that were not in the verification finding letter.
7. The Commission submitted that the VAT (Remission) (Official Aid Funded Projects) Order, 2003 of the *Value Added Tax Act* (Chapter 476 of the Laws of Kenya) (Repealed) ("VAT Act (Repealed)") stipulates the conditions that need to be met prior to zero-rating the services, which includes evidence of remission/exemption certificates and which the Respondent did not provide. The Commissioner contended that it restricted VAT in accordance with the provisions of section 17(6)(c) of VAT Act, 2013.

The Respondent's Submissions

8. The Respondent submits that the applicability of VAT to its two projects is clearly set out under the VAT laws applicable during the period reviewed by the Commissioner, that is, the VAT Act, 2013 and the VAT Act (Repealed). The Respondent therefore urges the Court to determine whether the services listed in the invoices assessed by the Commissioner qualify as zero rated services under the VAT laws and whether the Respondent performed all procedural requirements that have been set out in order to qualify for zero rating of the above invoices.
9. The Respondent contends that the Commissioner erred in assessing an additional output tax of KES 35,551,088.00 relating to KenHA and Ministry of Roads projects by reclassifying them as standard rated instead of zero rated. The Respondent submits that the Commissioner ignored the fact that the services in the Kisumu-Kakamega road construction and Mass Rapid Transit System projects were financed by International Development Association and African Development Fund respectively and that this fact is evident in their respective contract agreements that were signed on 8th November 2012 and 20th January 2014 respectively.
10. It further contends that the taxation of these projects from a VAT perspective cut across the transition period from the VAT Act (Repealed) to the current VAT Act, 2013 which commenced on 2nd September 2013. The Respondent states that sections 2 and 3 of the Value Added Tax (Remission)



(Official Aid Funded Projects) Order, 2003 of the VAT Act (Repealed) and section 68(4) and (4A) of the VAT Act, 2013 are the relevant legislative provisions that guide the taxation of official aid-funded projects and that its projects qualified for VAT remission before and after 2nd September 2013.

11. The Respondent further submits that the contract for Merille-Marsabit Road project was between the Ministry of Transport and its non-resident head office in Germany and that it is an autonomous foreign branch of its head office in Germany and only reports income from projects executed using its local resources. Further, the Merille-Marsabit road is under the Respondent's head office and all revenue arising from this project is entirely reported in Germany.
12. The Respondent also submits that upon the taking effect of the VAT Act, 2013 the law confirmed that tax remissions will still apply on all, "official aid-funded projects, with an express provision in their agreements for the remission of tax on any taxable goods or services supplied for the implementation of the project, where the agreement was concluded before the commencement of this Act". It points out that this has been captured as the only requirement for zero rating under section 68 of the VAT Act, 2013 for projects that commenced prior to 2nd September 2013.
13. The Respondent maintains that the grant of these remissions was substantially evident in letters received by the Respondent, responding to enquiries on the zero rating of the projects, from the Ministry of Transport addressed to the National Treasury and Kenya Revenue Authority confirming that the exemption of these projects is in line with the guidelines for VAT exemption of Official Aid Funded projects as per the Treasury Circular Ref No. DFN 415/232/011 dated 4th October 2012. The Respondent submits that it is on this basis that invoices raised to KeNHA and the Ministry of Roads by the Respondent were not subjected to VAT

Analysis and Determination

14. The main issue falling for determination is whether the Tribunal erred in determining that the Respondent's projects were official aid funded projects and thus exempted from VAT as they qualified for zero-rating. It is apparent from the submissions that the issue is one of interpretation and application of the statutory provisions hence is it important to recall the strictures of section 56(2) of the *Tax Procedures Act, 2015* ("TPA") which provides that, "An appeal to the High Court or to the Court of Appeal shall be on a question of law only".
15. Following the Supreme Court decision in *Gatirau Peter Munya v Dickson Mwenda Kithinji and 2 Others [2014] eKLR*, the Court of Appeal in *John Munuve Mati v Returning Officer Mwingi North Constituency & 2 others [2018] eKLR* summarised what amounts to "matters of law" as follows:

[38] The interpretation or construction of the Constitution, statute or regulations made thereunder or their application to the sets of facts established by the trial Court. As far as facts are concerned, our engagement with them is limited to background and context and to satisfy ourselves, when the issue is raised, whether the conclusions of the trial judge are based on the evidence on record or whether they are so perverse that no reasonable tribunal would have arrived at them. We cannot be drawn into considerations of the credibility of witnesses or which witnesses are more believable than others; by law that is the province of the trial court.
16. As stated, the Commissioner charged VAT on the services offered by the Respondent for its projects to KenHA and the Ministry of Transport/Roads for the reason that the Respondent did not provide exemption certificates as required by the VAT Act, 2013.
17. The applicable provisions in dealing with this issue are common ground. Paragraphs 2, 3, 4 and 5 of the Value Added Tax (Remission) (Official Aid Funded Projects) Order, 2003 of the VAT Act (Repealed) provided as follows:



2. The whole of the tax payable on taxable services, materials and equipment, including vehicles, which the Commissioner is satisfied are for use in the construction, equipping or execution of an aid funded project, to be, or in the process of being carried out pursuant to an agreement between the Government and a foreign government, or a foreign or international agency, institution, foundation or organization, supplying or making available aid funds, materials or equipment (in this Order referred to as “the aid agency”) is remitted subject to the conditions set out in paragraph 3
3. The conditions referred to in paragraph 2 are that—
 - (a) the agreement expressly provides for remission of tax on taxable services, materials and equipment, including vehicles;
 - (b) the agreement provides that—
 - (i) the materials and equipment, including vehicles, shall become the property of the Government, any public university, the Kenya Medical Research Institute, the Kenya Bureau of Standards or such other non-profit making organization in Kenya as the Minister may, by notice in the Gazette, specify for the purposes of this Order; or
 - (ii) the materials and equipment belong to, and whilst in Kenya, continue to belong to the aid agency; or
 - (iii) that both the conditions specified in this subparagraph apply;
 - (c) the implementing agency shall, at all reasonable times, make the records of the materials and equipment available to an authorized officer and shall give the officer every facility necessary to inspect and audit such records;
 - (d) within ninety days after the completion of the project, the aid agency shall provide the Commissioner—
 - (i) in the case of a situation referred to in subparagraph (b)(i), with a detailed list of items of equipment which have been used in the execution of the project and which, not forming part of the project itself, have become the property of the Government or other organization referred to in that subparagraph;
 - (ii) in the case of a situation referred to in subparagraph (b)(ii), with a detailed list of items of equipment which have been used in the execution of the project and which remain the property of the aid agency; and
 - (e) the Commissioner may, if he considers it necessary, inspect the project at any time during its execution
4. The remission of tax under paragraph 2 shall not apply to—
 - (a) fuels and oils for use in vehicles and equipments for the projects:
Provided that the Minister may grant remission under this subparagraph after taking into consideration the terms and conditions of the funding agreement;
 - (b) all taxable services, except those specified in any remission Order published under section 23 of the Act.



5. Notwithstanding the provisions of paragraph 2, tax shall become payable if goods which are the subject of this Order are used or disposed of in a manner inconsistent with the purpose for which the remission is granted.
18. Section 2 of the VAT Act (Repealed) and of the VAT Act, 2013 define an, “official aid funded project” as “a project funded by means of a grant or concessional loan in accordance with an agreement between the Government and any foreign government, agency, institution, foundation, organisation or any other aid agency”.
19. Section 68(4) and (4A) of the VAT Act, 2013 provides for the transitional and savings provisions of the VAT Act (Repealed) as follows:
- (4) Where a remission of tax was granted under the repealed Act on any taxable goods or services, such remission shall continue to remain in force for a period of five years from the date of commencement of this Act.
- (4A) For the avoidance of doubt and despite any other provision of this Act or other written law for the time being in force, the expression “remission of tax” in subsection (4) shall, in the case of an official aid-funded project, be deemed to include express provision in the agreement in respect of that project for the remission of tax on any taxable goods or services supplied for the implementation of the project, where the agreement was concluded before the commencement of this Act;
- Provided that a remission to which this subsection applies shall remain in force for a period of five years with effect from the commencement of this subsection.
20. Since resolution of this matter concerns the interpretation of a tax legislation, the statute must be looked at using slightly different lenses as the language imposing the tax must receive a strict construction leaving no room for intendment or implication (see *Cape Brandy Syndicate v I.R. Commissioners [1921] 1KB*, *Mount Kenya Bottlers Ltd & 3 others v Attorney General & 3 others NRB CA Civil Appeal No. 164 of 2013 [2019] eKLR* and *Stanbic Bank Kenya Limited v Kenya Revenue Authority CA Civil Appeal No. 77 of 2008 [2009] eKLR*).
21. From the provisions I have cited above, more so Paragraphs 3 and 4 of the Value Added Tax (Remission) (Official Aid Funded Projects) Order, 2003 of the VAT Act (Repealed), I do not find any provision or condition that required the Respondent to satisfy the Commissioner through exemption certificates that the project qualifies for remission. Acceding to the Commissioner’s position that exemption certificates were necessary, would amount to amending the clear language of the statute particularly where there is clear evidence that the tax payer has met the conditions imposed by the statute and regulations to entitle it to remission of tax. It is not disputed that the subject projects were Official Aid Funded Projects and if at all there was any doubt, the letter dated 4th October 2012 from the Ministry of Finance to the Commissioner was a clear confirmation.
22. It is also not in doubt that for the Respondent to benefit from the remission, it had to take some procedural steps that ought to have been taken by the Respondent and the relevant line Ministry. From the record, and the Tribunal found as a fact, that the Respondent submitted all that was required from it in order to be fully compliant and have its remission request approved. I agree with the Tribunal on this front and the finding that having discharged its duty by applying for remission, it had a legitimate expectation that the remission would be granted.

Conclusion and Disposition



23. For the reasons I have set out above, I affirm the Tribunal's findings that the subject projects were Official Aid Funded Projects and that as such, they qualified for remission and that the Respondent properly applied for remissions. I also do not find any fault in the Tribunal directing the Respondent to complete the process of obtaining the exemption certificates through the line Ministry. This order is consistent with the right to the Respondent to expect fair administrative action from State agencies protected in Article 47 of the *Constitution*.
24. The appeal is dismissed with costs to the Respondent.

DATED and DELIVERED at NAIROBI this 3rd day of NOVEMBER 2021.

D. S. MAJANJA

JUDGE

Court Assistant: Mr M. Onyango.

Ms Chelanga instructed by Kenya Revenue Authority for the Commissioner of Domestic Taxes.

Mr Agwara instructed by Munyaka Advocates LLP for the Respondent.

